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Special points of interest:

- Industrial output suffers record 8.5% decline in November
- Japanese firms have spent a record $78 bn abroad in 2008, but what about deals going the other way?
- Special reports: The unique experience of Japanese hot springs, and Joseph Deiss rewarded for his services to Swiss-Japanese relations

Inside this issue:

Japan's current economic situation

Reflecting the general mood throughout the globe, news from the Japanese economy have continued to be rather grim.
Following results showing that consumer confidence fell to the lowest level ever recorded, the Cabinet Office believes that Japan's economy is now "worsening rapidly".
This assessment came as the Japanese industry suffered an 8.5% month-on-month fall in output in November, the most rapid since the current index was introduced in 1953. Bankruptcies in 2008 have also increased by 11% from 2007 to 15,646, the first time the figure topped 15,000 in five years. Of those, 33 were listed companies, the highest number since the end of World War II. This led unemployment to rise to a seasonally adjusted 3.9%. The cabinet predicts unemployment will hit 4.7% in the fiscal year starting April this year.
Meanwhile, the current account surplus shrank for the ninth straight month in November, down 65.9% from a year earlier. Exports dropped 26.5%, the fastest pace of decline since comparable data became available in 1985, while imports were down 13.7%. Consumer price inflation also fell fast, the core CPI index having decreased from 1.9% in October to 1% in November.

Industrial production index (2008)
Source: Ministry of Economy, Trade and Industry (METI)

Japan's economy as a whole contracted in the second and third quarters of 2008, and the cabinet estimates that the economy will record a growth of only 0.1% in the coming fiscal year.
The pessimistic view comes as the parliament is set to start deliberating a record-high ¥88.55 trillion budget for fiscal 2009.

Japan aims to increase inflow of foreign capital

Judging by the number of foreign acquisitions they made, 2008 has been a good year for Japanese firms. They have indeed spent a record $77.8 billion abroad, more than three times the $23.5 billion of 2007. Of course, last year was not just like any other year: the financial crisis provided many cheap targets for the relatively sound Japanese banks to buy. In fact, last year's largest deal was

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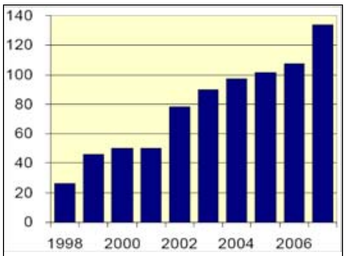
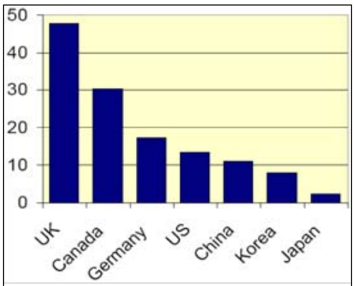


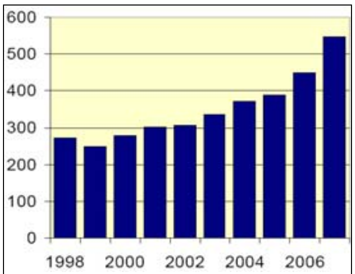
Japanese inward FDI stock ($bn)
Source: JETRO

Japan aims to increase inflow of foreign capital



Inward FDI stocks as a percentage of GDP (2007)
Source: Ministry of Foreign Affairs (MOFA)

The Japanese government has set out the target of doubling FDI as a percentage of GDP from 2.5% in 2006 to 5% in 2010.



Japanese outward FDI stock ($bn)
Source: JETRO

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Mitsubishi UFJ Financial Group's $9 billion acquisition of a 21% stake in Morgan Stanley.

Yet this surge in foreign acquisitions seems to signal a change in the Japanese mindset. While the strong yen and cheap targets were undoubtedly big factors behind last year's record spending, Japanese firms' increasing confidence in cross-border M&A is not to be dismissed.

Not only have they become quicker at executing deals, they have also begun winning auctions for public companies. Their post-acquisition attitude has also become more professional. While they used to take time and seemed hesitant in their decision-making once a foreign firm was theirs, Japanese firms have recently become more efficient in the integration process.

Following its $8.8 billion acquisition of US biotech firm Millennium Pharmaceuticals, Takeda Pharmaceutical paid retention bonuses to many Millennium employees to make sure they stay on for at least 12 months.

Yet, while Japanese firms are splashing their cash abroad, deals going the other way have been much rarer. In 2008, total inward M&A plunged to $28.3 billion from $57 billion the year before. While it is hard to see a trend in these figures in the past few years, it is fair to claim that Japan has not yet fully embraced incoming M&A activities, as some still see foreign buyers as intruders trying to harm venerable local companies.

Nonetheless, there are some positive signs. Most importantly, the government has identified M&A as one of the prime methods of promoting investment in Japan. Several reforms have thus taken place, with the revision of the Corporation Law – which now allows triangular mergers, in which a foreign company's Japanese subsidiary can use its parent company's shares to buy a local company – representing a major development. Japanese firms have also pledged to adopt International Financing Reporting Standards (IFRS) by 2011, and the use of defense mechanisms such as poison pills has also been on a steady decline in the past few years.

In fact, these recent developments go beyond M&A, and highlight the willingness by Japanese authorities and business leaders to increase overall foreign investment into Japan. Indeed, with a total inward FDI stock of ¥15.4 trillion, or about 3% of GDP at the end of 2007, Japan's figures remain far behind other major economies. At the end of 2006, FDI in the UK was 44.6% of GDP, while that of France was 33.2%.

In response, the Japanese government has set out the target of doubling FDI as a percentage of GDP from 2.5% in 2006 to 5% in 2010.

A nationwide program is currently being implemented to achieve this goal. In addition to the promotion of inwards M&A, the program includes plans to improve the transparency and understandability of regulations on foreign capital as well as the establishment of a plan to reduce overall business costs, especially Japan's high corporate tax rate.

Furthermore, the government has implemented several sector- and location-specific priority strategies. For instance, the medical device and pharmaceutical sector is considered a strategic sector to which FDI should be directed because of Japan's 'device lag', a 5-10 year delay in adopting certain products. Because investors often favor the Tokyo area, the government has also pushed for the promotion of investments into Japan's other regions, a task JETRO is actively taking part in.

Through programs of this kind, Japan's traditional reluctance towards FDI and M&A is slowly making way for a new mindset. Japanese people increasingly understand the positive impact FDI can make, through additional jobs, new technologies, or new business models, and this can only be good news for foreign investors.

The relaxing experience of Japanese hot springs

As a tourist visiting Japan, one of the highlights of your trip will certainly be the experience of taking a bath in one of the country's numerous hot springs, or *onsen*. The feeling it procures, as well as the profoundly Japanese nature of this thousand-year old custom have made it a favorite among tourists, both foreign and Japanese.

A volcanically active country, Japan counts over 26,000 hot springs, and experts say that with current drilling techniques, it is now possible to get mineral water almost anywhere in the archipelago.

While onsen were traditionally used as public bathing spaces, they have now mainly become tourist spots, even though they still play a major part in the lives of many Japanese.

Traditionally located outdoors, most onsen now have indoor baths as well. The change of attitudes since the opening of Japan to the West during the Meiji period also transformed onsen from traditionally mixed to single-sex (*i.e.* men and women bathe separately).

A recent trend has also seen the emergence of modern hot spring complexes, which offer a range of baths, massage services, sauna, etc. These are particularly popular in Tokyo, where they often retrieve the water from a depth of more than a kilometer below sea level.

Yet onsen are best enjoyed when spending a night at a *ryokan* (traditional Japanese inn) far from the stress of the big cities, where the excellent food, the stay in a traditional *tatami* room and the quietness of the place go hand-in-hand with the relaxing bathing experience. This is not only one of the most popular holiday activities among the Japanese, but is also highly recommended to any foreign visitor.

While Japan has become a truly modern society, onsen offer the chance to experience a more traditional side of the country.

Monkeys taking a bath in Jigokudani hot spring, Nagano Prefecture

Joseph Deiss receives highest award from Emperor

On November 5 last year, former Federal Councillor Joseph Deiss was awarded 'The Grand Cordon of the Order of the Rising Sun', the highest distinction a foreigner can receive, from the hands of Japan's Emperor Akihito.

The first Swiss to receive this honor, Joseph Deiss was rewarded for his services to the strong economic relations Japan and Switzerland have experienced in the past years. In particular, he has played a vital goal in the creation of the Free Trade and Economic Partnership Agreement (FTEPA) between the two countries upon which an agreement in principle was reached last September. It was back in 2004 that Jospeh Deiss, then President of the Swiss Confederation, laid the foundations for this agreement during a visit in Tokyo, by convincing Japan's Emperor, Prime Minister, Minister of Economy and Minister of Finance to start a feasibility study on the FTEPA.

Switzerland is the first European country to make such an agreement with Japan. Japan is also Switzerland's largest trading partner in Asia after China, with exports to Japan of CHF 6.7 billion and imports of CHF 3.5 billion in 2007. The relationship in terms of FDI is not bad either: with the Swiss FDI stock in Japan at CHF 13.7 billion at the end of 2007, Japan is the largest recipient of Swiss investments in Asia.

Joseph Deiss believes that the two nations have a lot in common, so that cooperation has come very naturally. He regards the distinction he received as a token of friendship from the Japanese people. And with the FTEPA due to be signed this year, economic relations between Switzerland and Japan have a bright future ahead.

Joseph Deiss with his distinction at the Imperial Palace in Tokyo

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JETRO is a government-related organization that works to promote mutual trade and investment between Japan and the rest of the world. Originally established in 1958 to promote Japanese exports abroad, JETRO's core focus in the 21st century has shifted toward promoting foreign direct investment into Japan and helping small to medium size Japanese firms maximize their global export potential.

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Survey on the operating profit of Japanese affiliated firms in six ASEAN countries and India

JETRO conducted a survey of Japanese Affiliated Firms operating in six ASEAN countries (Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam) and India. Firms were asked about their prospects for operating profits in 2008 and outlook for 2009. The survey revealed that business sentiment had worsened (compared to last year's survey) in many locations.
Among respondent firms in manufacturing sectors, reasons for worsened prospects for operating profits in 2008 relate mainly to higher energy and resource prices, with most citing "increased procurements costs" (66.8% of respondents), followed by "increased fuel and utility (electricity and gas) costs" (49.1%) and "insufficient passing on of costs" (36.5%).
Looking at business sentiment in industrial sectors with high concentrations of Japanese firms, the biggest losers were: transport equipment sectors in India (-61.4) and Thailand (-37.2), and the electrical and electronics sector in Malaysia (-28.2).
Respondent firms in non-manufacturing sectors generally expect worsened performance compared to last year, pointing to "sales declines in the local market" (46.9%), "increased personnel costs" (33.7%) and "increased fuel and utility costs" (32.0%). As with firms in manufacturing, non-manufacturers are also being hurt by consumers' reluctance to buy and higher personnel costs, in line with worsening inflation.

For more information, please go to:
http://www.jetro.go.jp/en/news/announcement/20081226299-news